



Tuesday, 16 October 2018

Rates: Fragile “recovery” on stock markets

Asian stock markets gain up to 1% despite a late downleg on Wall Street. Risk sentiment is improving following last week’s sudden correction, but the balance remains very fragile. Core bond’s performance was/is rather disappointing, suggesting the upside might be exhausted. The rising US budget deficit warrants a higher US credit risk premium going forward.

Currencies: Dollar to profit if global tensions were to ease?

Yesterday, the dollar lost slightly ground as sentiment on risk remained fragile. This morning, global equities are looking for a bottom after the recent correction and so does the dollar. Sentiment on the dollar might improve in a day-to-day perspective, but for now we don’t see a trigger to break out of the established ranges.

Calendar

Headlines

- **US equity markets** lost ground again on Monday with tech shares underperforming. **Asian markets** opened this morning with gains, with China excluded. All Chinese equity indices are currently losing ground.
- **Italy’s populist coalition government has approved the 2019 budget** that will widen the budget deficit to 2.4% of GDP. It will lower the retirement age and introduce payments to poor Italians. The EU is reviewing it this week.
- **The US budget deficit hits \$779bn during US President Trump’s first full fiscal year, a 6-yr high.** That’s \$113bn higher than last year, reaching 3.9% of US GDP. The deficit is expected to swell further, passing \$1tn by 2020.
- **Boris Johnson, former UK foreign minister, warned for a Brexit in name only.** He said the UK must be able to vary tariffs and strike trade deals after Brexit, otherwise it would “betray the British people”.
- **German Chancellor Angela Merkel has vowed to restore trust in her government** after her CDU’s sister party CSU tumbled down to its worst election result in almost 70 years.
- **China’s CPI rose 2.5% in September** from a year earlier, meeting market expectations and faster than the 2.3% inflation of August. **The PPI rose 3.6%**, higher than the 3.5% expectation but lower than the 4.1% in August.
- **Today’s eco calendar** contains the UK labour market report, US industrial production and German ZEW investor sentiment. SF Fed Daly speaks, Germany taps the bond market and more Q3 earnings will be released.

S&P	↘
Eurostoxx 50	↘
Nikkei	↑
Oil	↗
CRB	↗
Gold	↗
2 yr US	↗
10 yr US	↗
2yr DE	↗
10 yr DE	↗
EUR/USD	↗
USD/JPY	↘
EUR/GBP	↗

Rates

Fragile “recovery” of stock markets

	US yield	-1d
2	2,86	0,00
5	3,02	-0,01
10	3,16	-0,01
30	3,35	0,00

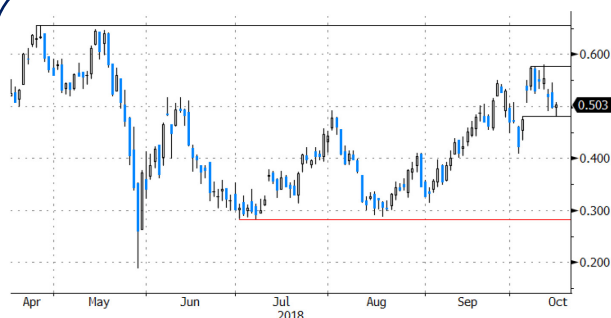
	DE yield	-1d
2	-0,57	-0,01
5	-0,09	0,00
10	0,50	0,01
30	1,13	0,01

Global core bonds ended nearly unchanged yesterday. The Bund opened stronger on more equity weakness early in European trading, but **stock markets soon found their composure**, putting the Bund on a slight downwardly sloping path. **Headline US retail sales disappointed, but details suggested a solid end to Q3 from a consumption point of view.** Core bonds didn't react. US equity markets sold off in the final trading hour, but the US Note future didn't profit from safe haven flows overnight.

The German yield curve steepened in a daily perspective with yield changes ranging between -0.8 bps (2-yr) and +0.6 bps (30-yr). US yield differences varied between +0.2 bps and -0.6 bps with the belly of the curve outperforming the wings. 10-yr yield spread changes vs Germany ended barely unchanged with Portugal (-5 bps; rating upgrade from junk Ba1 to investment grade Baa3) and Italy (-4 bps) outperforming. **The Italian government approved the controversial draft budget for next year (deficit of 2.4% of GDP) after European close.** It will now be reviewed by the EC who can ask to make changes, which would be a precedent. Spanish bonds underperformed Italian BTP's yesterday as the **Spanish government also decided to use more fiscal leeway than earlier agreed with Europe in its budget proposal.**

Asian stock markets ignore the late WS down leg and record gains of up to 1% overnight. **The US Note future loses ground. The US budget deficit officially rose to 3.9% of GDP during US President Trump's first full fiscal year** which is the highest since 2012. The CBO forecasts it to rise even further in the years ahead. **These deteriorating US fiscal metrics warrant higher US yields via a higher credit risk premium going forward and adds to our longer term bearish US Note future call.**

Today's eco calendar contains September US industrial production and October German ZEW investor sentiment. We don't expect them to be game changers today. **We'd rather continue monitoring developments on stock markets following last week's bearish break of some European indices. We add though that core bond's performance was rather disappointing last week given circumstances, indicating that the upside might be exhausted.** Comments from SF Fed governor Daly could be interesting if she touches on monetary policy given that she's new at the Fed (didn't participate in September meeting).



German 10-yr yield : early October gap higher is closed



US 10-yr yield retested previous 3.12% resistance

Currencies

R2	1,2155	-1d
R1	1,1996	
EUR/USD	1,1579	0,0019
S1	1,1510	
S2	1,1448	

R2	0,91	-1d
R1	0,9052	
EUR/GBP	0,8804	0,0013
S1	0,8628	
S2	0,8548	

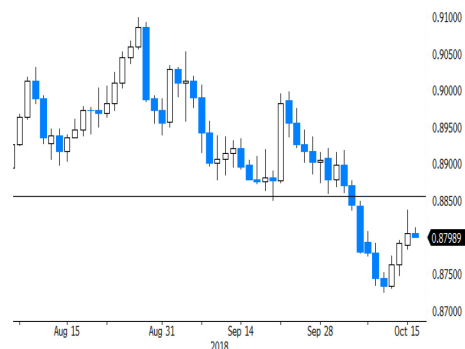
Dollar apparently needs easing of tensions

On Monday, FX traders still had to navigate a series of uncertainties, both economic and political in nature. **Even so, the moves in the major dollar cross rates were confined to established ranges.** The focus stayed on the US-China trade tensions and on the rift between the US and Saudi-Arabia on the disappearance of journalist Kashoggi. The USD proved again vulnerable to these topics. On **the eco side of the story**, US retail sales weren't really convincing. EUR/USD retested the 1.16 area and the trade-weighted dollar slipped to the 95 area. US equities held in negative territory for most of the session, but there was no obvious link with the dollar. EUR/USD finished the session at 1.1570 (from 1.1560). USD/JPY lost some further ground on global risk off to finish at 111.77. **This morning**, Asian equities mostly show modest gains with China underperforming. The jury is still out but rumours/headlines suggests that the US and Saudi Arabia are looking to avoid and escalation of the tensions. **The dollar is trading marginally stronger.** USD/CNY (6.9250 area) is holding near the recent top. EUR/USD trades around 1.1570. The **kiwi dollar** (NZD/USD) profits from higher than expected Q3 CPI data. **Later today**, ZEW economic confidence will be published in Germany. **In the US**, the production data and the NAHB housing indicator will be published. The data will probably only be of intraday significance for USD trading. **Global sentiment will remain key for FX trading.** Of late, we adopted a neutral bias on the dollar (EUR/USD). We still see no clear trigger for EUR/USD to break out of the 1.1432/1.1815 ST range. **If geopolitical tensions were to ease and if equities would finally show some tentative signs of bottoming, higher US yields might also provide some support to the dollar in a day-to-day perspective.**

Yesterday morning, sterling declined as EM-UK Brexit talks this weekend ended in a stalemate. However, the reaction was modest. EUR/USD settled in the low 0.88 area as FX traders awaited the next political developments. Today, UK labour data will be published. **Wage data always have market moving potential.** However, the focus remains on Brexit ahead of the EU Summit later this week. EU policy makers are likely to repeat that a deal is possible. However, of late, sterling traders reacted modestly to 'brexit noise'. Sterling probably needs 'hard news'/concrete steps for a real directional move. **Unless that happens, more technical driven wait-and-see action might be on the cards.**



USD (Trade-weighted- DXY): holding within established range. Dollar to rebound of global sentiment improves?



EUR/GBP: sterling traders stay in wait-and-see modus, looking for 'real news' on BRExit

Calendar

Tuesday, 16 October		Consensus	Previous
US			
15:15	Industrial Production MoM (Sep)	0.2%	0.4%
15:15	Capacity Utilization (Sep)	78.2%	78.1%
15:15	Manufacturing (SIC) Production (Sep)	0.2%	0.2%
16:00	NAHB Housing Market Index (Oct)	66	67
16:00	JOLTS Job Openings (Aug)	6900	6939
22:00	Total Net TIC Flows (Aug)	\$60.3b	\$52.2b
22:00	Net Long-term TIC Flows (Aug)	--	\$74.8b
UK			
10:30	Claimant Count Rate (Sep)	--	2.6%
10:30	Jobless Claims Change (Sep)	--	8.7k
10:30	Average Weekly Earnings 3M/YoY (Aug)	2.6%	2.6%
10:30	Weekly Earnings ex Bonus 3M/YoY (Aug)	2.9%	2.9%
10:30	ILO Unemployment Rate 3Mths (Aug)	4.0%	4.0%
10:30	Employment Change 3M/3M (Aug)	15k	3k
EMU			
11:00	Trade Balance SA (Aug)	14.7b	12.8b
11:00	ZEW Survey Expectations (Oct)	--	-7.2
Germany			
11:00	ZEW Survey Current Situation (Oct)	74.4	76.0
11:00	ZEW Survey Expectations (Oct)	-12	-10.6
China			
03:30	PPI YoY (Sep)	3.6%A	4.1%
03:30	CPI YoY (Sep)	2.5%A	2.3%
Events			
Q3 earnings	Blackrock (12:15), Johnson & Johnson (12:45), Morgan Stanley (13:00), Goldman Sachs (13:30), Netflix (22:05) ...		
11:30	Germany to Sell EUR4 Bln 0% 2020 Bonds		
22:15	San Francisco Fed's Daly Speaks at Wellesely College		

10-year	<u>Close</u>	<u>-1d</u>		2-year	<u>Close</u>	<u>-1d</u>	Stocks	<u>Close</u>	<u>-1d</u>
US	3,16	-0,01		US	2,86	0,00	DOW	25250,55	-89,44
DE	0,50	0,01		DE	-0,57	-0,01	NASDAQ	7430,744	-66,15
BE	0,89	0,00		BE	-0,49	0,00	NIKKEI	22549,24	277,94
UK	1,61	-0,02		UK	0,82	-0,02	DAX	11614,16	90,35
JP	0,15	0,00		JP	-0,11	0,00	DJ euro-50	3210,37	15,96
IRS	<u>EUR</u>	<u>USD</u>	<u>GBP</u>	EUR	<u>-1d</u>	<u>-2d</u>	USD	<u>-1d</u>	<u>-2d</u>
3y	0,08	3,12	1,29	Eonia	-0,3690	-0,0010			
5y	0,42	3,14	1,47	Euribor-1	-0,3690	0,0000	Libor-1	2,2798	0,0000
10y	1,04	3,21	1,71	Euribor-3	-0,3180	0,0000	Libor-3	2,4364	0,0000
				Euribor-6	-0,2660	0,0010	Libor-6	2,6521	0,0000
Currencies	<u>Close</u>	<u>-1d</u>		Currencies	<u>Close</u>	<u>-1d</u>	Commodities	<u>Close</u>	<u>-1d</u>
EUR/USD	1,1579	0,0019		EUR/JPY	129,42	-0,27	CRB	199,74	1,80
USD/JPY	111,77	-0,44		EUR/GBP	0,8804	0,0013	Gold	1230,30	8,30
GBP/USD	1,3152	-0,0001		EUR/CHF	1,1432	-0,0043	Brent	80,78	0,35
AUD/USD	0,713	0,0016		EUR/SEK	10,367	0,0082			
USD/CAD	1,2991	-0,0033		EUR/NOK	9,4413	-0,0374			

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Contacts

Brussels Research (KBC)		Global Sales Force	
Mathias Van der Jeugt	+32 2 417 51 94	Corporate Desk(Brussels)	+32 2 417 45 82
Peter Wuyts	+32 2 417 32 35	Institutional Desk(Brussels)	+32 2 417 46 25
Mathias Janssens	+32 2 417 51 95	CBC Desk (Brussels)	+32 2 547 19 19
Dieter Lapeire	+32 2 417 25 47	France	+32 2 417 32 65
Dublin Research		London	+44 207 256 4848
Austin Hughes	+353 1 664 6889	Singapore	+65 533 34 10
Shawn Britton	+353 1 664 6892		
Prague Research (CSOB)		Prague	
Jan Cermak	+420 2 6135 3578		+420 2 6135 3535
Jan Bures	+420 2 6135 3574		
Bratislava Research (CSOB)		Bratislava	
Marek Gabris	+421 2 5966 8809		+421 2 5966 8820
Budapest Research		Budapest	
David Nemeth	+36 1 328 9989		+36 1 328 99 85

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